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Takeshita Prepared For Washington

Prime Minister Noboru Takeshita has been busily preparing for his first trip to Washington as head of state January 12. As a matter of course, the preparations cover defense, foreign policy and economic matters, but Mr. Takeshita has painstakingly prepared his domestic audience as well as his foreign hosts.

Accompanied by Foreign Minister Sosuke Uno, the prime minister will spend three days each in the United States and Canada, returning home January 20 after stopping in Hawaii. Mr. Takeshita has a full itinerary planned for his Washington stay. On January 12 Mr. Uno meets with Secretary of State George Shultz. The prime minister's January 13 schedule includes a meeting with President Reagan, a ceremonial visit to the tomb of the unknown soldier, an afternoon discussion with House of Representative leaders, and a state dinner at the Japanese Embassy. On his final day the prime minister will deliver an address at the National Press Club and visit with Senate members before holding a press conference with the Japanese press.

new ideas. Agricultural issues could also pose thorny problems since farmers remain politically powerful and are adamantly opposed to further liberalization. The prime minister cannot go too far in supporting U.S. defense and foreign policies without risking a domestic backlash. During talks with opposition party leaders before leaving, Mr. Takeshita agreed that Japan will not over-extend itself in these areas.

Mr. Takeshita will have to prove himself to both domestic and foreign audiences. While his first trip abroad to attend a meeting of the Association of Southeast Asian Nations in December 1987 met with favorable reaction, the U.S.-Japan relationship is far more critical and sensitive. He may prove a disappointment to Americans if he maintains his image as a quiet, consensus-oriented and conservative politician. He may disappoint Japanese voters if he acts otherwise, however. The new prime minister must maintain a precarious balance, a position to which he is accustomed.

Jon Choy

Nervous Markets Push Yen Back Down

Just when it was beginning to look like betting against the U.S. currency was the safest gamble around, the inevitable happened: the dollar rose and the yen dropped. In the space of a few days in early January the yen gave up almost all of the gains it had made in December.

As 1988 opened few were forecasting a dollar rally, but once it had happened there were numerous explanations. Some experts said it was a technical correction. Others pointed out that many firms in need of dollars had sat on the sidelines, hoping to catch the dollar's bottom before making the purchases they would have to make eventually anyway. This theory suggested that once the dollar stopped dropping it would inevitably rise. Most intriguing, there were reports in Europe and Japan that the world's central bankers had a secret plan to keep exchange rates within fairly narrow bands. Consistent with this view, Tokyo, Washington and other governments reportedly continued intervening on the side of the dollar even after it started recovering, casting doubt on those who felt that all the central bankers and finance ministers wanted to do was slow the dollar's decline.

Still the dollar remains in one of its weakest positions ever. Last year was another rough one, as Table 1 illustrates. It was clear that the dollar could drop again on even the most trivial bad news. For the second time in a row it ended the year by hitting a new bottom.

The dollar's drop, which dates from early 1985, barely shows the effect of several well-publicized efforts to alter or stabilize its value. In September 1985 the Group of Five industrial nations met at the Plaza Hotel in New York. Their agreement that the dollar was overvalued now seems like a dramatic understatement.

In February 1987 the group, having added two members, met again in Paris and worked out what has become known as the Louvre Accord. This time the goal was to stabilize exchange rates. Japan and Germany agreed to stimulate their economies and the United States said it would cut its budget deficit. Japan

had just lowered the discount rate to 2.5 percent, where it remains; Germany followed with a later cut. Japan also implemented new government spending measures. Both steps have served to stimulate domestic demand, and the lower interest rates in Japan made U.S. investments attractive, thereby helping to sustain the value of the dollar.

Table 1: Yen-Dollar Exchange Rate, 1982-87

(monthly average, Tokyo interbank market)

	1982	1983	1984	1985	1986	1987
January	Y224.6	Y232.9	Y234.0	Y254.1	Y200.0	Y154.5
February	Y235.2	236.3	233.7	260.3	184.6	153.5
March	240.7	237.9	225.5	258.4	178.8	151.5
April	244.9	237.7	225.0	251.7	175.6	143.0
May	236.5	234.8	230.7	251.6	166.9	140.5
June	251.0	240.1	233.3	249.0	167.8	144.5
July	255.1	240.5	242.7	241.7	158.7	150.2
August	258.8	244.4	242.2	237.2	154.1	147.6
September	262.7	242.7	245.2	236.9	154.8	143.0
October	271.4	233.0	246.9	214.8	156.0	143.5
November	265.1	235.3	243.3	203.9	162.7	135.3
December	242.5	234.3	248.0	202.8	162.1	128.4
Annual Average	249.1	237.5	237.5	238.5	168.5	144.6

Despite general agreement that Japan has pursued an expansionary monetary and fiscal policy, officials in different countries have criticized both Bonn and Washington for doing too little. In any case the dollar dropped after the Louvre Accord, but then appeared to stabilize, as planned. There were reports over the summer that the central banks intervened to keep the dollar from rising more. Whether intended or not, higher interest rates here worked to support the dollar, as the prime rate, which had been dropping since early 1986, started moving up in April.

By early fall whatever was propping the dollar up began to fail. Higher interest rates in the United States and increasing intervention by the Bank of Japan in August, September and early October were not enough to support the dollar. After the October stock market crash here and abroad, itself partly a consequence of the dollar support actions, U.S. policy changed abruptly, as Washington now accepted what it had paid so dearly to try to prevent -- ever lower values for the currency. With the Louvre Accord apparently dead, the rest of the world had little choice but to go along.

In 1987 foreign exchange markets may have seemed calmer to the Japanese than to the Americans. While the yen generally appreciated against the currencies of Japan's major trading partners, its rise against the dollar was the most dramatic, as Table 2 shows. Generally the yen increased most against third currencies that are explicitly linked to the dollar (the Hong Kong dollar) or that are closely tied by trade (the Canadian dollar). Until it reversed direction late in the year, the yen fell against the British pound and the Taiwan dollar.

Table 2: Changes in the Yen Against Selected Currencies

(other currencies in terms of yen at the end of year)

	1986	1987	Percent Change
German mark	Y83.26	Y78.21	6.5%
British pound	239.41	233.86	2.4
Australian dollar	106.59	91.34	16.7
Canadian dollar	117.06	96.14	21.8
Korean won	0.19	0.16	18.8
Singapore dollar	73.94	62.34	18.6
Taiwan dollar	4.55	4.31	5.6
Hong Kong dollar	20.69	16.27	27.2
U.S. dollar	161.60	124.05	30.3

With so many having managed to lose so much money, the months after Black Monday have been marked by extreme nervousness in the currency markets. Because of the approaching presidential election, Washington is likely to continue to see a weak and declining dollar as a lesser evil than rising interest rates, higher taxes, or reduced government spending -- the perceived alternatives. While still trying to figure out the stock market crash, currency traders will soon have to focus on what seems like the distant future -- political leadership in Washington after November. It will be an exciting year.

Douglas Ostrom

European Community Lists U.S. Trade Barriers

In December the European Community published its third annual list of U.S. trade barriers, naming over 30 obstacles maintained by the United States. The list is a counterattack on the congressionally mandated National Trade Estimate compiled annually by the Office of the U.S. Trade Representative. The U.S. report was first published in 1985 in compliance with Section 303 of the 1984 Trade Act, which requires an annual account of the most important trade barriers affecting U.S. exports of goods and services, American investment abroad and intellectual property rights -- whether or not they are consistent with international trading rules (see JEI Report No. 43B, November 11, 1987).

Critics charge that the USTR's document ignores U.S. trade barriers, thereby presenting a misleading picture of American trade practices. In order to achieve a more accurate representation of the international trade scene, the EC published its first list of American barriers to EC exports in December 1985, just a few months after the first National Trade Estimate was released. "The purpose of the EC report is to make clear that trade practices which impede exports are not a unique problem faced only by U.S. exporters. EC exporters face similar problems when trading with the U.S," the community's report charges.